

*Revised*  
**OPEN MEETING  
MEMORANDUM**

TO: THE COMMISSION

FROM: Utilities Division

DATE: March 31, 2022

RE: IN THE MATTER OF THE APPLICATION OF TUCSON ELECTRIC POWER COMPANY FOR THE ESTABLISHMENT OF JUST AND REASONABLE RATES AND CHARGES DESIGNED TO REALIZE A REASONABLE RATE OF RETURN ON THE FAIR VALUE OF THE PROPERTIES OF TUCSON ELECTRIC POWER COMPANY DEVOTED TO ITS OPERATIONS THROUGHOUT THE STATE OF ARIZONA AND FOR RELATED APPROVALS. (DOCKET NO. E-01933A-19-0028)

SUBJECT: APPLICATION FOR AUTHORIZATION FOR ANNUAL PURCHASED POWER AND FUEL ADJUSTMENT CLAUSE RATE ADJUSTMENT

## INTRODUCTION

Enclosed are the Commission Staff's memorandum and proposed order for the Application for Authorization for Annual Purchased Power and Fuel Adjustment Clause Rate Adjustment (Docket No. E-01933A-19-0028). This is only a Staff recommendation to the Commission; it has not yet become an order of the Commission. The Commission can decide to accept, amend or reject Staff's proposed order.

You may file comments to the recommendation(s) of the proposed order by e-filing at <https://efiling.azcc.gov/> or filing an original and the appropriate number of copies in accordance with the Filing Requirements available at <http://azcc.gov/hearing/docket-control-center-filing-requirements>, with the Commission's Docket Control on or before: **April 8, 2022**.

This matter may be scheduled for Commission deliberation at its Open Meeting scheduled **April 12, 2022, and April 13, 2022**.

If you have any questions about this matter, please contact Brian K. Bozzo of our Staff at (602) 542-0852, or Elijah Abinah, Director, at (602) 542-6935.

## BACKGROUND

On February 1, 2022, Tucson Electric Power Company ("TEP" or "Company") filed its updated calculations and a request for authorization for a Purchased Power and Fuel Adjustment



Clause ("PPFAC") rate adjustment in accordance with the PPFAC Plan of Administration ("POA"). The current PPFAC rate, approved in Decision No. 77960, dated April 15, 2021, is \$0.003294 per Kilowatt-hour ("kWh"). The Company is proposing to set the PPFAC rate at \$0.018424 per kWh for the period April 1, 2022, through March 31, 2023. TEP's overall PPFAC bank balance is currently about \$108 million under-collected.

The PPFAC rate consists of a Forward Component and a True-up Component. The Forward Component consists of the forecasted fuel and purchased power costs for the year, usually commencing on April 1 and ending on March 31 of the following year, less the average base rate of \$0.029053 per kWh approved in Decision No. 77856. The True-up Component is a reconciliation of any over- or under-recovered amounts from the preceding PPFAC year to be credited to, or recovered from, customers in the following PPFAC year.

### STAFF ANALYSIS AND RECOMMENDATIONS

TEP's 2022 PPFAC balance reflects a number of items, including two years of cost deferrals and delayed recoveries. Due to the COVID-19 pandemic, the implementation of the PPFAC rate resets in 2020 and 2021 were delayed. Similar to TEP's 2020 PPFAC, the 2021 PPFAC rate included 1) \$13.5 million of fuel and purchased power costs incurred in 2020 that were shifted for future collection and 2) a total of \$4.3 million of additional PPFAC costs relating to a two-month delay in the implementation date (from April 1, 2021, to June 1, 2021). As a result of these unrecovered costs, TEP's current PPFAC balance includes \$17.8 million of prior year costs that would have normally been recovered in 2021. These deferred cost items are shown below:

Description	Amount
Fuel and purchased power costs from 2020 that were shifted for future collection.	\$13.5 million
Two-month delay in implementation date (April 1, 2021, to June 1, 2021) creating additional PPFAC cost.	\$4.3 million
<b>Total Under-collection of PPFAC - Shifted Costs</b>	<b>\$17.8 million</b>

TEP's application outlines that a number of external factors contributed to the magnitude of the Company's PPFAC costs to be recovered in the current application. In addition to the \$17.8 million in shifted costs, TEP described \$90 million in higher costs as contributing to the \$108 million PPFAC bank balance.

When natural gas and wholesale power prices declined through 2018, the 2019 TEP PPFAC rate reflected a substantial decrease from the previous year rate. Afterward, summer market conditions reversed, and periods of drastically higher prices were experienced. The volatile market resulted in significant under-collections and a higher forward component in 2020.

Significant wholesale power and natural gas market volatility continued after 2019. The application states that the San Juan Basin natural gas prices increased an average of 88 percent between December 2020 and December 2021, and the average Palo Verde wholesale power



prices in June and July of 2021 increased by 179 percent compared to 2020. TEP also entered into summer purchased power agreements, due to summer capacity shortages and power flow issues, to secure firm capacity and ensure reliability during the hot summer months. Weather events such as the heat wave of June 2021 and winter storm Uri in February 2021 led to additional unforeseeable costs due to record high natural gas and power prices.

In addition, replacement power purchases were made in 2020 and 2021 as a result of planned and unplanned generation outages. TEP experienced higher transmission costs due to the new 250 Megawatt Oso Grande wind project in New Mexico, which began commercial operation in 2021.

*2022 Purchased Power and Fuel Adjustment Clause Rate Calculation*

Since the implementation of the 2021 PPFAC rate was delayed and not set to recover the full costs of fuel and purchased power, those costs were included in the new yearly balance, thereby creating an increase in the PPFAC rate in 2022. The current and proposed PPFAC component rates are shown in the table below.

**TEP Proposed PPFAC Rate Calculation (\$/kWh)**

<b>PPFAC Rate Calculation</b>	<b>Current Rate (6/1/21)</b>	<b>Proposed Rate (4/1/22)</b>	<b>Change</b>
Forward Component Rate	\$0.001778	\$0.006219	\$0.004441
True-up Component Rate	\$0.001516	\$0.012205	\$0.010689
PPFAC Rate	\$0.003294	\$0.018424	\$0.015130

According to TEP, the proposed PPFAC rate would increase average residential bills by \$12.68 per month. For the average residential customer, the proposed PPFAC rate would appear as a \$14.68 surcharge per month (797 kWh x \$0.018424 per kWh). The TEP proposed \$12.68 per month bill impact represents recovery of the under-collection over a 12-month period.

The Company provided the Commission with two additional options for the True-up component to help mitigate the bill impact for its customers. Option 1 would provide six additional months for recovery of the PPFAC bank balance and Option 2 would provide 12 additional months for the bank balance recovery.

On February 18, 2022, Freeport Minerals Corporation docketed a request seeking the establishment of an annual \$0.004 per kWh cap on TEP's PPFAC Adjustor rate. Arizona Public Service Company ("APS") currently has such a cap as part of its adjustor mechanism. Staff recognizes that APS and TEP have different base costs of power and different existing fuel and purchased power adjustor rates. Therefore, the impact of a cap to each company's balance recovery will vary. Staff does not believe Freeport Minerals Corporation's request for a cap is



appropriate. By implementing a cap, the customers will end up paying more in the future because of the balance being carried forward plus the interest component rather than paying the balance now. However, Staff understands the benefit of a longer recovery period and is recommending a longer time period.

The bill impacts, PPFAC rate components and true-up collection scenarios for 12, 18, 24, and 30 months options are summarized in the tables below.

True-Up Balance Recovery Period	Avg. 2022 Estimated Residential Monthly Bill Impact
12 Months (POA)	\$12.68
18 Months	\$9.27
24 Months	\$7.56
30 Months	\$6.54

Recovery Period	Forward	True-Up	Total 2022 PPFAC Rate
12 Months (POA)	\$0.006219	\$0.012205	\$0.018424
18 Months	\$0.006219	\$0.008137	\$0.014356
24 Months	\$0.006219	\$0.006103	\$0.012322
30 Months	\$0.006219	\$0.004882	\$0.011101

PPFAC True-Up Collection Scenarios	2022	Estimated Balance Shifted to 2023
12 Months (POA)	\$108 million	\$ 0
18 Months	\$72 million	\$36 million
24 Months	\$54 million	\$54 million
30 Months	\$43 million	\$65 million

Staff has reviewed the forecast and calculations provided by the Company and found them to be reasonable. However, the pandemic posed an unprecedented challenge for ratepayers, and Staff currently believes that the option to recover over 18 months will best serve the public interest while still allowing for some recovery for TEP. Staff therefore recommends the Forward Component rate be set at \$0.006219 per kWh, and the True-up Component rate be set at \$0.008137 per kWh, resulting in a PPFAC rate of \$0.014356 per kWh, effective the first billing cycle after the effective date of this Decision. Staff's recommended PPFAC rate calculation is shown below.



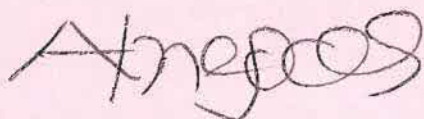
**Staff-Recommended PPFAC Rate Calculation**

PPFAC Rate Calculation	Current Rate (6/1/21)	Proposed Rate (4/1/22)	Change
Forward Component Rate	\$0.001778	\$0.006219	\$0.004441
True-up Component Rate	\$0.001516	\$0.008137	\$0.006621
PPFAC Rate	\$0.003294	\$0.014356	\$0.011062

Staff's recommended PPFAC rate would increase average residential bills by \$9.27 per month. For the average residential customer, the proposed PPFAC rate would appear as a \$11.44 surcharge per month (797 kWh x \$0.014356 per kWh). The \$9.27 per month bill impact defers a portion of the recovery of the under-collection from customers who are challenged by the continuing effects of the COVID-19 pandemic and other economic issues.

The PPFAC has a balancing account, which means any over- or under-collected balance has interest applied annually. Any over-collection or under-collection existing at the end of the PPFAC year will be credited/debited an amount based on the one-year Nominal Treasury Constant Maturities rate contained in the Federal Reserve Statistical Release H-15 on the first business day of the calendar year. The interest rate as of January 3, 2022, was 0.40 percent.

Staff recommends that TEP file in Docket Control a revised Statement of Charges consistent with the Decision in this case within 30 days of the effective date of the Decision.



Elijah O. Abinah  
Director  
Utilities Division

EOA:BKB:elr\SJE

ORIGINATOR: Brian K. Bozzo



THE COMMISSION

March 31, 2022

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On this 31st day of March, 2022, the foregoing document was filed with Docket Control as a Utilities Division Memorandum & Proposed Order, and copies of the foregoing were mailed on behalf of the Utilities Division to the following who have not consented to email service. On this date or as soon as possible thereafter, the Commission's eDocket program will automatically email a link to the foregoing to the following who have consented to email service.

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THE COMMISSION

March 31, 2022

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Edna Luna Reza  
Administrative Support  
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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

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Chairwoman

3 SANDRA D. KENNEDY

Commissioner

4 JUSTIN OLSON

Commissioner

5 ANNA TOVAR

Commissioner

6 JIM O'CONNOR

Commissioner

7 IN THE MATTER OF THE APPLICATION )  
8 OF TUCSON ELECTRIC POWER )  
9 COMPANY FOR THE ESTABLISHMENT )  
10 OF JUST AND REASONABLE RATES AND )  
11 CHARGES DESIGNED TO REALIZE A )  
12 REASONABLE RATE OF RETURN ON )  
13 THE FAIR VALUE OF THE PROPERTIES )  
14 OF TUCSON ELECTRIC POWER )  
COMPANY DEVOTED TO ITS )  
OPERATIONS THROUGHOUT THE )  
STATE OF ARIZONA AND FOR RELATED )  
APPROVALS. )

DOCKET NO. E-01933A-19-0028

DECISION NO. \_\_\_\_\_

ORDER

**APPLICATION FOR AUTHORIZA-  
TION FOR ANNUAL PURCHASED  
POWER AND FUEL ADJUSTMENT  
CLAUSE RATE ADJUSTMENT**

15 Open Meeting  
16 April 12 and 13, 2022  
17 Phoenix, Arizona

18 BY THE COMMISSION:

19 FINDINGS OF FACT

20 **Background**

21 1. On February 1, 2022, Tucson Electric Power Company ("TEP" or "Company") filed  
22 its updated calculations and a request for authorization for a Purchased Power and Fuel Adjustment  
23 Clause ("PPFAC") rate adjustment in accordance with the PPFAC Plan of Administration ("POA").  
24 The current PPFAC rate, approved in Decision No. 77960, dated April 15, 2021, is \$0.003294 per  
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28 ...



2. The PPFAC rate consists of a Forward Component and a True-up Component. The Forward Component consists of the forecasted fuel and purchased power costs for the year, usually commencing on April 1 and ending on March 31 of the following year, less the average base rate of \$0.029053 per kWh approved in Decision No. 77856. The True-up Component is a reconciliation of any over- or under-recovered amounts from the preceding PPFAC year to be credited to, or recovered from, customers in the following PPFAC year.

#### **Staff Analysis and Recommendations**

3. TEP's 2022 PPFAC balance reflects a number of items, including two years of cost deferrals and delayed recoveries. Due to the COVID-19 pandemic, the implementation of the PPFAC rate resets in 2020 and 2021 were delayed. Similar to TEP's 2020 PPFAC, the 2021 PPFAC rate included 1) \$13.5 million of fuel and purchased power costs incurred in 2020 that were shifted for future collection and 2) a total of \$4.3 million of additional PPFAC costs relating to a two-month delay in the implementation date (from April 1, 2021, to June 1, 2021). As a result of these unrecovered costs, TEP's current PPFAC balance includes \$17.8 million of prior year costs that would have normally been recovered in 2021. These deferred cost items are shown below:

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4. TEP's application outlines that a number of external factors contributed to the magnitude of the Company's PPFAC costs to be recovered in the current application. In addition to the \$17.8 million in shifted costs, TEP described \$90 million in higher costs as contributing to the \$108 million PPFAC bank balance.

5. When natural gas and wholesale power prices declined through 2018, the 2019 TEP PPFAC rate reflected a substantial decrease from the previous year rate. Afterward, summer market conditions reversed, and periods of drastically higher prices were experienced. The volatile market resulted in significant under-collections and a higher forward component in 2020.



6. Significant wholesale power and natural gas market volatility continued after 2019. The application states that the San Juan Basin natural gas prices increased an average of 88 percent between December 2020 and December 2021, and the average Palo Verde wholesale power prices in June and July of 2021 increased by 179 percent compared to 2020. TEP also entered into summer purchased power agreements, due to summer capacity shortages and power flow issues, to secure firm capacity and ensure reliability during the hot summer months. Weather events such as the heat wave of June 2021 and winter storm Uri in February 2021 led to additional unforeseeable costs due to record high natural gas and power prices.

7. In addition, replacement power purchases were made in 2020 and 2021 as a result of planned and unplanned generation outages. TEP experienced higher transmission costs due to the new 250 Megawatt Oso Grande wind project in New Mexico, which began commercial operation in 2021.

*2022 Purchased Power and Fuel Adjustment Clause Rate Calculation*

8. Since the implementation of the 2021 PPFAC rate was delayed and not set to recover the full costs of fuel and purchased power, those costs were included in the new yearly balance, thereby creating an increase in the PPFAC rate in 2022. The current and proposed PPFAC component rates are shown in the table below.

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10. The Company provided the Commission with two additional options for the True-up component to help mitigate the bill impact for its customers. Option 1 would provide six additional months for recovery of the PPFAC bank balance and Option 2 would provide 12 additional months for the bank balance recovery.

11. On February 18, 2022, Freeport Minerals Corporation docketed a request seeking the establishment of an annual \$0.004 per kWh cap on TEP's PPFAC Adjustor rate. Arizona Public Service Company ("APS") currently has such a cap as part of its adjustor mechanism. Staff recognizes that APS and TEP have different base costs of power and different existing fuel and purchased power adjustor rates. Therefore, the impact of a cap to each company's balance recovery will vary. Staff does not believe Freeport Minerals Corporation's request for a cap is appropriate. By implementing a cap, the customers will end up paying more in the future because of the balance being carried forward plus the interest component rather than paying the balance now. However, Staff understands the benefit of a longer recovery period and is recommending a longer time period.

12. The bill impacts, PPFAC rate components and true-up collection scenarios for 12, 18, 24, and 30 months options are summarized in the tables below.

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24 Months	\$7.56
30 Months	\$6.54

Recovery Period	Forward	True-Up	Total 2022 PPFAC Rate
12 Months (POA)	\$0.006219	\$0.012205	\$0.018424
18 Months	\$0.006219	\$0.008137	\$0.014356
24 Months	\$0.006219	\$0.006103	\$0.012322
30 Months	\$0.006219	\$0.004882	\$0.011101

PPFAC True-Up Collection Scenarios	2022	Estimated Balance Shifted to 2023
12 Months (POA)	\$108 million	\$ 0
18 Months	\$72 million	\$36 million
24 Months	\$54 million	\$54 million
30 Months	\$43 million	\$65 million



13. Staff has reviewed the forecast and calculations provided by the Company and found them to be reasonable. However, the pandemic posed an unprecedented challenge for ratepayers, and Staff currently believes that the option to recover over 18 months will best serve the public interest while still allowing for some recovery for TEP. Staff therefore recommends the Forward Component rate be set at \$0.006219 per kWh, and the True-up Component rate be set at \$0.008137 per kWh, resulting in a PPFAC rate of \$0.014356 per kWh, effective the first billing cycle after the effective date of this Decision. Staff's recommended PPFAC rate calculation is shown below.

**Staff-Recommended PPFAC Rate Calculation**

<b>PPFAC Rate Calculation</b>	<b>Current Rate (6/1/21)</b>	<b>Proposed Rate (4/1/22)</b>	<b>Change</b>
Forward Component Rate	\$0.001778	\$0.006219	\$0.004441
True-up Component Rate	\$0.001516	\$0.008137	\$0.006621
PPFAC Rate	\$0.003294	\$0.014356	\$0.011062

14. Staff's recommended PPFAC rate would increase average residential bills by \$9.27 per month. For the average residential customer, the proposed PPFAC rate would appear as a \$11.44 surcharge per month (797 kWh x \$0.014356 per kWh). The \$9.27 per month bill impact defers a portion of the recovery of the under-collection from customers who are challenged by the continuing effects of the COVID-19 pandemic and other economic issues.

15. The PPFAC has a balancing account, which means any over- or under-collected balance has interest applied annually. Any over-collection or under-collection existing at the end of the PPFAC year will be credited/debited an amount based on the one-year Nominal Treasury Constant Maturities rate contained in the Federal Reserve Statistical Release H-15 on the first business day of the calendar year. The interest rate as of January 3, 2022, was 0.40 percent.

16. Staff recommends that TEP file in Docket Control a revised Statement of Charges consistent with the Decision in this case within 30 days of the effective date of the Decision.

...

...



CONCLUSIONS OF LAW

1. Tucson Electric Power Company is an Arizona public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution.

2. The Commission has jurisdiction over Tucson Electric Power Company and the subject matter of the application.

3. The Commission, having reviewed the application and Staff's Memorandum, concludes that it is in the public interest to reset the Purchased Power and Fuel Adjustment Clause rate as discussed herein.

ORDER

IT IS THEREFORE ORDERED that the change in the Purchased Power and Fuel Adjustment Clause rate to \$0.014356 per kWh is hereby approved.

IT IS FURTHER ORDERED that the new Purchased Power and Fuel Adjustment Clause rate shall go into effect the first billing cycle after the effective date of this Decision.



1 IT IS FURTHER ORDERED that Tucson Electric Power Company file in Docket Control a  
2 revised Statement of Charges consistent with the Decision in this case within 30 days of the effective  
3 date of the Decision.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5  
6 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

7  
8  
9 CHAIRWOMAN MÁRQUEZ PETERSON

COMMISSIONER KENNEDY

10  
11 COMMISSIONER OLSON

COMMISSIONER TOVAR

COMMISSIONER O'CONNOR

12  
13 IN WITNESS WHEREOF, I, MATTHEW J. NEUBERT,  
14 Executive Director of the Arizona Corporation Commission,  
15 have hereunto, set my hand and caused the official seal of this  
16 Commission to be affixed at the Capitol, in the City of  
17 Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2022.

18 \_\_\_\_\_  
19 MATTHEW J. NEUBERT  
EXECUTIVE DIRECTOR

20 DISSENT: \_\_\_\_\_

21  
22 DISSENT: \_\_\_\_\_

23  
24 EOA:BKB:elr/SJE



Tucson Electric Power Company  
Docket No. E-01933A-19-0028

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